

Message Text

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SUBJ: NORTH SEA OIL DEVELOPMENT 1974

REF: EDINBURGH AIRGRAM A-18 RE UK PARLIAMENTARIANS MEETING

AT STATE DEPARTMENT DECEMBER 30-31 ON OIL TAXATION AS
SEEN FROM SCOTLAND, THE FOLLOWING NORTH SEA OIL DEVELOPMENTS
IN 74 MERIT SPECIAL ATTENTION:

1. ACCORDING TO ALISTAIR DUNNETT, CHAIRMAN OF OCCIDENTAL-GETTY
GROUP AND EX-EDITOR SCOTSMAN, "EXCITEMENT HAS GIVEN WAY TO
DISAPPOINTMENT AND DISILLUSION", NOT BECAUSE OF LACK OF OIL
RESERVES, WHICH CONTINUE TO MOUNT, BUT BECAUSE OF POLITICAL,
INFLATIONARY, AND MECHANICAL PROBLEMS, WHICH HAVE RISEN EVEN
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FASTER.

2. RESERVES HAVE BEEN THE SOURCE OF HEATED DEBATE AMONG AND BETWEEN GOVERNMENT AND INDUSTRY EXPERTS WITH THE CURRENT ENERGY MINISTER ACCUSING HIS PREDECESSORS OF "GRIEVOUSLY AND DELIBERATELY" UNDERESTIMATING THE VALUE OF THE OIL DISCOVERED. THE DEPARTMENT OF ENERGY'S BROWN PAPER IN MAY ESTIMATED UK NORTH SEA RESERVES AT APPROX 1 BILLION TONS PROVEN, TWO BILLION PROBABLE AND THREE BILLION POSSIBLE. INDEPENDENT EXPERTS CLAIM THESE ARE SERIOUSLY UNDERESTIMATED, PROFESSOR ODELL (EX SHELL) CLAIMING THAT THE NORTH SEA WILL YIELD 15-20 BILLION TONS OR SOME HUNDRED MILLION BARRELS. THIS WOULD MEAN A POTENTIAL DAILY PRODUCTION OF 15-20 MBPD (WHICH ONLY SAUDI ARABIA IS CURRENTLY CAPABLE OF) RATHER THAN THE UKG ESTIMATE OF THREE MBPD. INDUSTRY ESTIMATES FALL BETWEEN THESE EXTREMES, THE MAJORS ON THE CONSERVATIVE SIDE, THE INDEPENDENTS MORE LIBERAL. THE MEAN WOULD FALL IN A LEAGUE WITH US AND USSR RESERVES, WHICH ARE ONLY EXCEEDED BY SAUDI ARABIA, IRAN AND KUWAIT. IN OTHER WORDS, NORTH SEA OIL IS A VITAL FACTOR IN WESTERN ECONOMIC SURVIVAL, IF, AS, AND WHEN IT LEAVES THE SUB-SURFACE OF THE SEA.

3. NORTH SEA DISCOVERIES HAVE ALSO CONTINUED TO MOUNT IMPRESSIVELY IN 74. AT LEAST FOUR AND POSSIBLY SIX "GIANT" FIELDS (OVER ONE-HALF BILLION BARRELS EACH) WERE DISCOVERED BY MID-YEAR. U.S. COMPANIES ARE HEAVILY INVOLVED IN VIRTUALLY ALL UK OIL FIELDS AND WERE ESTIMATED BY THE UKG TO HOLD 36.8 PERCENT SHARE IN EXISTING DISCOVERIES, COMPARED TO 41.2 PERCENT UK AND 11 PERCENT FRENCH. THREE COMPANIES, BP AND SHELL-ESSO HAVE MADE HALF OF THE DISCOVERIES (ESSO HAS NO INDEPENDENT PRESENCE IN UK EXPLORATION TO DATE BUT HAS OPTED TO WORK THROUGH SHELL IN THE NORTH SEA). AMOCO, CONOCO, OCCIDENTAL, MOBIL, PHILLIPS, UNOCAL, SIGNAL, GULF, AND TEXACO ARE ALL SUCCESSFUL U.S. OPERATORS. THE BULK OF THE DRILLING CONTRACTORS ARE AMERICAN, E.G. SANTA FE, SEDCO, ODECO, ZAPATA. TWO AMERICAN CONSTRUCTION COMPANIES, MCDERMOTT AND BROWN AND ROOT, HAVE A SMALLER SHARE OF THE PLATFORM AND PIPE LINE BUSINESS. OVER FIFTY AMERICAN COMPANIES ASSOCIATED WITH THE OIL INDUSTRY ARE CURRENTLY OPERATING IN SCOTLAND.

4. HENCE, WHY "DISAPPOINTMENT AND DISILLUSION" AS OF THE LAST
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SIX MONTHS. CONOCO VICE-PRESIDENT MAIER GAVE THE PRESS IN EDINBURGH SOME OF THE FOLLOWING REASONS:

A. EXTREME COST ESCALATION WHICH ADDED HUNDRED OF MILLIONS OF POUNDS TO ORIGINAL INVESTMENT FORECAST.

B. LIQUIDITY CRISES AND HIGH INTEREST RATES AROUND 13 PERCENT, PUT PARTICULAR STRAIN ON SMALLER OPERATORS.

C. FEARS AND UNCERTAINTY REGARDING SUPPOSED UK TAXATION AND PARTICIPATION MEASURES, INCLUDING THE THREAT OF

RETROACTIVITY;

D. INCREASING SCARCITY OF ESSENTIAL MATERIALS AND EQUIPMENT, DUE IN PART TO INCREASING COMPETITIVE ACTIVITY IN OTHER OFF-SHORE AREAS AROUND THE GLOBE, PARTICULARLY PROJECT INDEPENDENCE.

E. FAILURE OF SUPPLIERS TO MEET DELIVERY DEADLINES, PARTICULARLY IN BRITAIN, WHICH EXTENDED THE TIME TO COMPLETE PROJECTS AND TO GENERATE REVENUE REQUIRED FOR FURTHER DEVELOPMENT;

F. COMPLEXITY OF THE NORTH SEA STRUCTURE, WHICH MADE FORECASTS OF RESERVES AND PRODUCTION RISKY IN THE ABSENCE OF PRODUCTION AND DEVELOPMENT EXPERIENCE AND HISTORY;

G. ENVIRONMENTAL CONDITIONS WHICH, ASIDE FROM NORMAL DELAYS CREATED BY CONSCIENTIOUS ENVIRONMENTALISTS, WERE THE WORST IN DRILLING HISTORY.

H. HIGH ECONOMIC COST OF SIMULTANEOUS RESEARCH AND DEVELOPMENT, TRIAL AND ERROR. MAIER ADDED THAT WHEREAS THESE NEGATIVE FACTORS EXISTED ONE YEAR AGO, FEW HAD EXPECTED ALL TO SNOWBALL CONCURRENTLY;

5. OTHER RESULTS, NONE OF THE THREE FIELDS WHICH THE UKG ESTIMATED WOULD BE ON PRODUCTION THIS YEAR ARE YET ON STREAM, I.E. ARGYLL (HAMILTON), AUK (SHELL-ESSO) AND FORTIES (BP). THEY ARE APPROXIMATELY ONE YEAR BEHIND SCHEDULE AND MAY BE PRODUCING AT THE MOST 30,000 BPD, 30,000 BPD AND 80,000 BPD RESPECTIVELY IN TWELVE MONTHS. OTHERS ESTIMATE NO MORE THAN 20,000 BPD BY NEXT DECEMBER AND CLAIM THAT UK SELF-SUFFICIENCY IS NOW TWO TO THREE YEARS BEHIND SCHEDULE. CHATE, MANAGER OF SHELL, STATES THAT 25 INSTEAD OF AN EXPECTED 35 RIGS ARE NOW DRILLING IN THE NORTH SEA.

6. ESCALATION OF COSTS ARE AS MIND-BLOWING AS ELSEWHERE IN THE UK:

A. QUOTATIONS ON SEMI-SUBMERSIBLE RIGS NOW COSTING 9,600 UNCLASSIFIED

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POUNDS PER DAY ARE 18,750 POUNDS;

B. A PLATFORM ORDERED DECEMBER 73 COST 37 MILLION POUNDS INSTALLED; SAME DESIGN IN JUNE 74 COST 54 MILLION POUNDS;

C. FIELD DEVELOPMENT COSTS HAVE INCREASED FROM 800 MILLION POUNDS PER DAILY BARREL OUTPUT CAPACITY TO OVER 2,000 POUNDS TODAY OR SOME TWENTY TIMES MIDEAST OFF-SHORE COSTS AND TEN TIMES OFF-SHORE AFRICA. IT SEEMS THAT, LIKE ARABS, EVERYBODY IS CHARGING AND GOUGING WHAT THE MARKET WILL BEAR, WHICH IS EVEN EASIER WHEN MATERIALS ARE IN SHORT SUPPLY. CONOCO IN DUNDEE JUST PAID 800 DOLLARS FOR 120 DOLLARS MOORING ROPE BECAUSE THEY HAD TO HAVE IT IMMEDIATELY OR THEIR RIG WOULD HAVE SHUT DOWN AT 50,000 DOLLARS PER DAY. THE RECOMMENDATION HAS BEEN MADE HERE THAT THE USG AND/OR WESTERN GOVERNMENTS TOGETHER (IAE?) WILL HAVE TO DEVELOP A ROTATION SYSTEM FOR SCARCE ESSENTIAL EQUIPMENT, PARTICULARLY THAT MANUFACTURED IN THE U.S.

(DRILL STEMS, PIPE). IF ANY RATIONAL DEVELOPMENT AT ANY RATIONAL PRICE IS TO SURVIVE.

7. LASTLY, AND NEXT TO INFLATION, MOST IMPORTANT, IS GOVERNMENT TAX AND PARTICIPATION POLICY. FORTUNATELY, UNLIKE INFLATION, IT IS NOT YET OUT OF CONTROL AND DOES NOT DEPEND ON ARAB OR OTHER EXTERNAL FORCES. WASHINGTON AND LONDON ARE, OF COURSE, IN BETTER POSITION TO ASSESS THE SERIOUSNESS OF THIS ELEMENT IN AMERICAN COMPANY FEARS FOR THE FUTURE AND ANY RESTRAINTS RESULTING THEREFROM. THE INDUSTRY MAY BE UNDERGOING HEART ATTACKS IN BOARDROOMS AT HOME, BUT IN SCOTLAND THERE SEEMS TO BE LITTLE AFFECT WITHIN THE BRANCH OFFICES. BUSINESS IS BOOMING IN ABERDEEN WHERE THERE ARE THREE JOBS FOR ANY WARM BODY. THE EXCEPTIONS ARE THE BANKERS, INVESTMENT HOUSES AND VISITING EXECUTIVES, PARTICULARLY FROM THESE SMALL OUTFITS, ALL OF WHOM ARE PROFOUNDLY CONCERNED. THE LATTER FEAR PARTICULARLY THAT A SINGLE TAX RATE FOR LARGE AND SMALL FIELDS WILL RESULT IN THE LATTER NOT BEING PRODUCED. ALL COMPANIES FEAR RETRO ACTIVITY AND RENEGOTIATION OF LICENSES. NONE LIKE GOVERNMENT NATIONALISATION, SOCIALISATION OR PARTICIPATION, AND THE SMALLER ARE EXPECTED TO SUCCUMB ONE BY ONE IN THE LIQUIDITY CRISIS. CONTINUED UNCERTAINTY SURROUNDING LABOUR ACTIONS OBSTRUCT ALL COMPANIES PLANNING, EVEN THOUGH INDECISION IS BETTER THAN BAD DECISION. COMPANY OFFICIALS HERE APPROVE THE DIALOGUE TAKING PLACE WITH GOVERNMENT OFFICIALS, BUT FEAR THAT POLITICAL LEADERS, SUCH AS LORD BALOGH (LABOUR) AND BILLY WOLFE (SNP)

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HAVE ALREADY COUNTED THE CHICKENS BEFORE THE EGGS ARE LAID OR HATCHED, WOULD APPLY TO THE NORTH SEA AS PUNITIVE MEASURES AS OPEC APPLIES TO CALMER WATERS, AND LOOK TO NORWAY MORE AS A MODEL THAN A DOG IN THE WESTERN ECONOMIC MANGER. FORTUNATELY, OTHER CONCERNED AND COMPETENT PARLIAMENTARIANS AND CIVIL SERVANTS ARE ASKING SEARCHING QUESTIONS, SINCE IT IS EVIDENT TO AT LEAST A FEW THAT THE UK HAS NO OPTION BUT TO PRODUCE OIL ASAP. IT IS ON THESE MATTERS THAT THE JENKIN-FLETCHER VISIT TO THE U.S. IS BASED.

8. ACTION RECOMMENDATION: THAT THE DEPT DEVOTE AS MUCH THOUGHT TO THIS DIALOGUE AS NORTH SEA OIL RATES IN OUR ECONOMIC AND POLITICAL PHILOSOPHY, PARTICULARLY IF THERE IS ANY CONCERN THAT THE CRASH MAY ARRIVE BEFORE THE OIL.FUNKHOUSER

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